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INFO ALL EC CAPITALS 0160

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DEPT PASS AGRICULTURE FROM AGRICULTURAL ATTACHE

E.O. 11652: N/A

TAGS: EAGR, FR, EC, ECON

SUBJECT: EC POLICY AND POLITICAL IMPLICATIONS OF DROUGHT
IN FRANCE

REF: STATE 194278; TOFAS 248 (NOTAL)

1. SUMMARY: DESPITE PRESSURES ENGENDERED BY DROUGHT,
FRENCH AGRICULTURAL SECTOR, GOF, POLITICAL PARTIES AND
PUBLIC SHOW NO SIGNS OF RELAXING THEIR STRONG SUPPORT
FOR CAP POLICIES OF EC. PROJECTED DECREASED OUTFLOW OF
FEOGA FUNDS FROM DIMINISHED PAYMENTS FOR EXPORT SUBSI-
DIES AND INCREASED INFLOW FROM VARIABLE LEVY PAYMENTS
SERVE TO BALANCE INCREASED DEMANDS FOR SECTORAL ASSIS-
TANCE. INSTEAD OF VIEWING AVAILABILITY OF FOREIGN SUP-
PLIES (ESSENTIALLY FROM US) AS PROOF OF VIABILITY AND
DEPENDABILITY OF OPEN MARKET SYSTEM, FRENCH WILL CHOOSE
TO POINT TO NEED FOR EC SUPPORT OF LESS EFFICIENT FAR-

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MERS THROUGH PRICE POLICY TO PROVIDE PRODUCTION IN YEARS

OF DIFFICULTY, SUCH AS 1976, TO AVOID EVEN LARGER BALANCE OF PAYMENTS OUTFLOW AND DEPENDENCY OF FOREIGN SOURCES OF SUPPLY. REDUCED FARM INCOMES WILL HARDEN FRENCH POLITICAL OPPOSITLON TO NEGOTIATING ON AGRICULTURE IN MTN, BUT AT THE SAME TIME WEAKEN EC ARGUMENTS AS TO EFFECTIVENESS OF COMMODI AGREEMENTS AND PRICE SUPPORT SYSTEMS AS MEANS OF STABILIZING TRADE AND FARM INCOME. HOWEVER, DROUGHT COULD SERVE TO HASTEN RATIONALIZATION OF AGRI-CULTURE REDUCE NUMBER OF FARMS) AND THUS HAVE LONG RANGE IMPACT IN EVENTUALLY LEADING FRENCH TO FOLLOW MORE MARKET-ORIENTED AGRICULTURAL POLICIES.

2. GENERAL COMMENTS: POLICY AND POLITICAL IMPLICATIONS OF DROUGHT DEPEND ON MAGNITUDE OF LOSSES FOR BOTH FARMERS AND FRENCH ECONOMY TOGETHER WITH PERCEIVED ADEQUACY OF COMPENSATORY MEASURES UNDERTAKEN BY GOF, INCLUDING DEGREE TO WHICH THEY CAN OBTAIN FUNDS FROM EC. INTERNAL FRENCH POLITICAL TENSIONS WILL LIKELY OVERSHADOW POLITICAL IMPLICATIONS FOR EC, CONSIDERING THAT FRENCH LEFT IS READY TO ATTACK WHATEVER MEASURES MAY BE ADOPTED BY GOF. HAVING WON THE LAST PRESIDENTIAL ELECTION BY LESS THAN 2 PERCENT, CURRENT ADMINISTRATION IS KEENLY AWARE OF NEED TO KEEP FARM BLOC SOLIDLY IN THEIR CAMP. IF FRANCE DOES NOT RECEIVE EC ASSISTANCE, THE LEFT WILL BE ABLE TO EXPLIT POLICY DILEMMA CONFRONTING GOF. GIVEN CURRENT BUDGET DEFICIT AND ALREADY QUICKENING PACE OF INFLATION, COMPLETE AND "ADEQUATE" COMPENSATION FOR FARMERS WILL FUEL INFLATIONARY PRESSURES, THUS LEADING TO CHARGES BY LEFT OF ECONOMIC MISMANAGEMENT.

3. DROUGHT IMPACT ON FARM INCOME - THE GOF HAS PROMISED TO MAINTAIN INCOME OF FARMERS AT LAST YEAR'S LEVELS. THIS WAS ONLY "HALF A LOAF" TO FRENCH FARMERS WHO ALREADY SAW THEIR REAL INCOMES IN 1975 DECLINE 3.8 PERCENT FROM PREVIOUS YEAR. THUS 1976 WILL BE THIRD YEAR IN A ROW OF REAL INCOME LOSSES FOR FARMERS. AGMIN IS SENDING OUT QUESTIONNAIRES TO FARMERS TO DETERMINE THEIR LOSSES WITH "PRECISION" BY SEPTEMBER 15. SEVERAL FARM GROUPS CLAIM LOSSES AMOUNT TO 10 TO 15 BILLION FF; PRESS REPORTS AGRICULTURAL ECONOMISTS PLACE FIGURE AT 5 TO 9 BILLION LIMITED OFFICIAL USE

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FRANCS. AGATT OFFICE VIEWS LOWER END OF LATTER RANGE AS MORE LIKELY. WHEN INCOME OF ENTIRE AGRICULTURAL SECTOR IS TAKEN INTO CONSIDERATION, IT BECOMES DIFFICULT TO MEASURE LOSSES BECAUSE INCREASED DROUGHT-INDUCED SLAUGHTER OF CATTLE WILL RAISE BEEF PRODUCTION, AND FRUIT PRODUCTION WILL RISE SUBSTANTIALLY IN EXCESS OF FREEZE DEVASTATED PRODUCTION LAST YEAR. REAL FARM INCOME CAN BE SHOWN TO HAVE FALLEN MORE SHARPLY WHEN PRICE INFLATION

IS TAKEN INTO CONSIDERATION.

4. FRENCH ECONOMIC AND BUDGETARY SITUATION - ALTHOUGH IN FIRST HALF OF 1976 FRENCH ECONOMY HAD PASSED FROM RECESSION TO GROWTH, BUDGET IS IN HEAVY DEFICIT AND DROUGHT ADDS TO BURDEN. FRANCE HAD A 12 PERCENT INFLATION RATE IN 1975 AND 13 PERCENT IN 1974 (STATED AS ANNUAL RATES). 1975 BUDGET DEFICIT WAS 40 BILLION FF, BUT MOST OF THIS DEFICIT WAS TRANSFERRED TO 1976 BUDGET.

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IN 1975 INDUSTRIAL IMPORTS WERE UP AND AGRICULTURAL IMPORTS WERE DOWN. WE EXPECT DROUGHT WILL CAUSE INCREASE IN AGRICULTURAL IMPORTS AND THE IMPACT COULD CUT INDUSTRIAL IMPORTS IN 1976. DROUGHT ALSO CAUSED INCREASED USE OF PETROLEUM AND COAL FOR ELECTRICITY WHICH IS CURRENT EXPENSE THAT WAS NOT FORECAST. THUS, BEFORE FIGURING INTO BUDGET ANY FINANCIAL HELP TO FARMERS, COMES A

CARRYOVER DEBT OF 40 BILLION FF, AN ALREADY EXPECTED 10-11 PERCENT INFLATION, TWO PREVIOUS YEARS OF HIGH INFLATION, AND A 9 PERCENT DECREASE IN FRANC VALUE IN 1976.

5. POLITICAL IMPLICATIONS FOR FRANCE - THE HAZY FACTORS SURROUNDING DETERMINATION OF INCOME LOSS SUGGEST MANY POINTS OF DISPUTE WILL ARISE IN FULFILLING GOF'S PROMISES: WHAT PRICES WILL BE USED TO ESTIMATE LOSSES? WHICH PORTION OF AGRICULTURE AND WHICH FARMERS SHOULD RECEIVE HELP? WILL LARGE GRAIN PRODUCERS OF FRANCE'S FAVORED AGRICULTURAL AREAS BE REIMBURSED ON A PAR WITH LIMITED OFFICIAL USE

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SMALLER FARMERS? (THE SOCIALISTS AND COMMUNISTS CAN BE EXPECTED TO BE HEARD FROM ON THIS). WILL CATTLE RAISERS, WHO STAND TO LOSE MOST BECAUSE OF DISMAL FORAGE PRODUCTION (OVER 50 PERCENT BELOW NORMAL), BE REIMBURSED EVEN IF THEIR INCOME INCREASES TEMPORARILY BECAUSE OF FORCED SLAUGHTER OF BEEF AND DAIRY CATTLE? IT IS CLEAR THAT PRIME MINISTER CHIRAC, WHO GAVE UP AGRICULTURAL PORTFOLIO, IN NAME IF NOT FULLY IN FACT, IS TRYING TO ANSWER SOME OF THESE QUESTIONS FOR GOF AND TO SMOOTH WAY TO AN ACCEPTABLE PLAN. HE IS CURRENTLY TRAVELING TO MANY OF DEPARTMENTS OF FRANCE WHICH HAVE BEEN DECLARED DISASTER AREAS (53 TO DATE) AND IS MEETING WITH AGRICULTURAL GROUPS, CHAMBERS OF AGRICULTURE, LOCAL OFFICIALS AND OTHERS IN RELATION TO CURRENT SITUATION. PIERRE JOXE, SOCIALIST PARTY AGRICULTURAL EXPERT, AND COMMUNIST PARTY OF FRANCE HAVE MAINTAINED PRESSURE ON GOF BY DEMANDING IMMEDIATE AID TO AGRICULTURE, PARTICULARLY TO CATTLEMEN, PRIOR TO "STOCK-TAKING" WHICH HAS BEEN SET FOR SEPTEMBER 29. FNSEA (NATIONAL FARMERS' FEDERATION) AND OTHER FARM GROUPS HAVE SIMILARLY DEMANDED IMMEDIATE AID. IF CHIRAC CAN SUCCESSFULLY MANAGE TO DEVELOP A PLAN ACCEPTABLE TO FRENCH AGRICULTURE AND NOT EXCESSIVELY INFLATIONARY IN IMPACT, IT WILL BE IMPORTANT ACHIEVEMENT. IF BALL IS FUMLED, IT WILL SET STAGE FOR FURTHER ATTACKS BY FRENCH LEFT. IF GOF IS SUCCESSFUL IN OBTAINING MORE THAN TOKEN AID FROM EC IN HELPING ITS FARMERS, IT WILL FURTHER STRENGTHEN SUPPORT IN FRANCE FOR WHOLE CONCEPT OF CAP AND GIVE GOF MORE BACKBONE IN WITHSTANDING EFFORTS BY SPECIAL INTEREST GROUPS (PRODUCERS OF ORDINARY WINE, PEACH GROWERS) TO CUT OFF IMPORTS OF COMPETING PRODUCTS FROM OTHER EC MEMBER COUNTRIES. REFUSAL OF EC TO ASSIST MEANINGFULLY WOULD THROW BURDEN OF ASSISTANCE SQUARELY ON FRENCH BUDGET AND WOULD POSE DIFFICULT CHOICES INVOLVING HELP FOR FARMERS, INFLATION POLICY, AND POSSIBLE LEVYING NEW TAXES.

CHIRAC PLANS TO ANNOUNCE ON AUGUST 25 A SERIES OF MEA-

SURES DESIGNED TO HELP HARD-PRESSED CATTLE RAISERS (REPORT TO FOLLOW SEPTEL). AGMIN BONNET IS PREPARING FOR ANNOUNCEMENTS BY MEETING WITH WIDE VARIETY OF FARM LEADERS AND SPECIFICALLY WITH PRESIDENTS OF NATIONAL LIMITED OFFICIAL USE

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FARMERS' FEDERATION, YOUNG FARMERS' CONFEDERATION, CHAMBERS OF AGRICULTURE, AND AGRICULTURAL CREDIT CONFEDERATION. FINMIN FOURCADE HAS RETURNED TO PARIS TO COMPLETE WORK ON PACKAGE WHICH WILL BE PRESENTED TO PRESIDENT GISCARD PRIOR TO PROMULGATION. BALL IS CLEARLY IN COURT OF GOVERNMENT WHICH WISHES TO AVOID AT ALL COST A SITUATION WHICH WOULD ALLOW CATTLE RAISERS AND OTHER DROUGHT-AFFECTED FARMERS TO UNITE IN ANGER WITH WINE AND FRUIT GROWERS OF SOUTHERN FRANCE.

6. ATTITUDE RE SELF-SUFFICIENCY - FRANCE IS LARGELY SELF-SUFFICIENT IN TEMPERATE ZONE AGRICULTURAL PRODUCTS, FAR MORE SO THAN ITS EC PARTNERS, AND IS SECOND LARGEST EXPORTER OF AGRICULTURAL PRODUCTS IN WORLD. YET, IT WILL BE FURTHER THAN EVER FROM SELF-SUFFICIENCY IN IMPORTANT ANIMAL FEED AREA IN 1976/77 CROP YEAR. FOR FIRST TIME IN MANY YEARS, FRANCE WILL BECOME A NET IMPORTER OF COARSE GRAINS, AND DEPENDENCY ON IMPORTED OIL SEEDS FOR PROTEIN FOR ANIMAL FEEDING WILL CONTINUE. FRENCH ARE UNDOUBTEDLY RELIEVED THAT LARGE AND RELATIVELY REASONABLY PRICED SUPPLIES ARE AVAILABLE IN UNITED STATES. THERE IS NO INDICATION, HOWEVER, THAT THEY ARE WILLING TO CONCLUDE THAT THESE SUPPLIES ARE AVAILABLE BECAUSE OF SMOOTH OPERATION OF U.S. OPEN MARKET SYSTEM. FRENCH BELIEVE THAT WITHOUT CAP IN PLACE PRODUCTION FROM MARGINAL FAR-

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MERS WOULD NOT HAVE BEEN FORTHCOMING AND SHORTFALLS WOULD HAVE BEEN EVEN LARGER, LEADING TO AN EVEN HEAVIER BALANCE OF PAYMENTS REVERSAL. WE SEE NO CRACKS IN THIS COMMONLY PERCEIVED VIEW IN FRANCE.

7. POLICY IMPACT ON CAP - DROUGHT COULD LEAD TO MORE AMENABLE FRENCH TREATMENT OF CERTAIN SPECIFIC ISSUES IN CAP BUT NO CHANGE IN BASIC APPROACH. WITH DAIRY PRODUCTION FORECAST TO DECLINE IN FRANCE IN 1976 BY 4 PERCENT, SHORT-TERM QUESTIONS OF NFDM DISPOSAL AND TAX ON VEGETABLE OILS WILL BECOME LESS INTRACTABLE. CONCURRENTLY LONG-TERM BASIC REFORM OF DAIRY SECTOR OR REDUCTION IN BEEF IMPORT RESTRICTIONS BECOME LESS LIKELY. WE WOULD BE SURPRISED, MOREOVER, TO SEE FRENCH TAKE MORE FLEXIBLE POSITION ON BASIC QUESTIONS OF VARIABLE LEVIES AND EXPORT SUBSIDIES BECAUSE OF DROUGHT IMPACT. IT IS LIKELY THAT FRANCE WILL PUSH FOR SUBSTANTIALLY HIGHER GRAIN PRICES IN 1977 IN EC TO MAKE UP FOR INCOME LOSSES.
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PERCEIVED EFFICACY OF EC PRICE SUPPORT SYSTEM TO MAINTAIN FARM INCOMES WILL BE UNDERMINED TO SOME EXTENT, ESPECIALLY IF DIRECT SUBSIDIES MUST BE PAID FROM NATIONAL TREASURIES. RELATIVELY LARGE AMOUNT OF DIRECT SUBSIDIES AS OPPOSED TO "SOFT" LOANS WILL BE EXPLOITED AS VICTORY FOR LEFT WHICH HAS MAINTAINED THAT DIRECT PAYMENTS ESSENTIAL TO SAVE SMALL FARMERS.

8. BUDGETARY IMPLICATIONS FOR CAP - WHILE BALANCE OF PAYMENTS AND BUDGETARY IMPLICATIONS OF DROUGHT ARE PARTI-

CULARLY UNFORTUNATE FOR FRENCH, BUDGETARY IMPACT ON CAP COULD SERVE TO DIMINISH PRESSURE EMANATING FROM WITHIN EC ON FRENCH TO COMPROMISE ON CERTAIN KEY ISSUES. WITH LESS INTERVENTION EXPENDITURES ANTICIPATED FOR MILK (SOMEWHAT OFFSET BY HIGH BEEF INTERVENTION PURCHASES), LESS EXPENDITURES FOR DISPOSAL OF SURPLUS STOCKS THROUGH SUBSIDIES, AND INCREASED REVENUES FROM VARIABLE LEVIES ON IMPORTED FOODSTUFFS, FEOGA SHOULD BE IN MUCH BETTER SHAPE AT END OF 1976/77 THAN AT BEGINNING.(MAJOR UNKNOWN IS BUDGETARY DRAIN BECAUSE OF HIGHER MONETARY COMPENSATION AMOUNTS). THIS SHOULD HAVE DUAL EFFECT OF LESSENING FRG OPPOSITION TO COSTLY OPERATION OF CAP AND LESSENING URGENCY BEHIND EFFORTS TO PUT INTO PLACE STRUCTURAL REFORM PROGRAM FOR DAIRY SECTOR. IN FACT, FRENCH MAY VIEW ROSY BUDGETARY OUTLOOK OF FEOGA AS GOLDEN OPPORTUNITY TO TAP EC FUNDS FOR DIRECT PAYMENT TO DROUGHT AFFLICTED FARMERS - WHICH MEANS MOSTLY FRENCH FARMERS. THIS WOULD BE VERY IMPORTANT TO GOF IN VIEW OF SEVERE DOMESTIC BUDGETARY LIMITATIONS DUE TO CONFINEMENTS OF ANTL-INFLATION POLICIES.

9. POLITICAL IMPACT ON EC - DEPENDS ON LEVEL OF FEOGA FUNDS AND DEGREE TO WHICH EC SHARES BURDEN OF FINANCING LOSSES IN INDIVIDUAL COUNTRIES. IF FEOGA FUNDS HAVE INCREASED, AS WE BELIEVE THEY HAVE, YET EC FAILS TO ASSIST INDIVIDUAL COUNTRIES BECAUSE OF AVERSION TO DIRECT SUBSIDIES, EUROPEAN "SOLIDARITY" ON ECONOMIC FRONT MAY BE WEAKENED TO SOME EXTENT. THEN FUTURE REQUESTS BY SPECIAL INTEREST GROUPS FOR DIRECT ASSISTANCE AT NATIONAL LEVEL WOULD BE DIFFICULT TO RESIST POLITICALLY.
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10. IMPACT ON EC STRATEGY IN MTN - DROUGHT WILL LIKELY HARDEN EC ARGUMENTS THAT AGRICULTURE IS A SPECIAL SECTOR, UNIQUELY SUBJECT OF VAGARIES OF NATURE, AND THEREFORE NEGOTIATIONS ON AGRICULTURE MUST BE CONSIDERED IN DIFFERENT CONTEXT THAN INDUSTRY.

EC ALSO LIKELY TO BE EVEN MORE RELUCTANT TO NEGOTIATE ON AGRICULTURE, ARGUING THAT IT HAS JUST SUFFERED MAJOR INCOME LOSSES AND THAT TRADE CONCESSIONS REQUIRING MAJOR SECTORAL ADJUSTMENTS WILL BE IMPOSSIBLE POLITICALLY AS BOTH RELATIVE AND ABSOLUTE LOSSES WILL BE INFLICTED ON LIBERALIZED SECTORS. GIVEN EC AGRICULTURAL INCOME PROSPECTS FOR 1976/77, EC VERY LIKELY ARGUE THAT "1977 MTN PACKAGE" INCLUDE ONLY INDUSTRY AND THAT AGRICULTURE BE INCLUDED IN "LATER" NEGOTIATIONS WHEN INCOME CONDITIONS IMPROVE.

ABILITY OF EC TO "CONVERT" OTHERS TO ITS CONCEPT OF "HARMONIZATION" OF PROTECTION LEVELS AND "ORGANIZATION" OF AGRICULTURAL MARKETS VIA COMMODITY AGREEMENTS WITH NARROW PRICE BANDS WILL BE DIMINISHED IF LARGE DIRECT SUBSIDIES MUST BE PAID FROM NATIONAL TREASURIES. HOWEVER, IF LOSSES FINANCED MAINLY FROM FEOGA FUNDS, THIS WILL BE

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CONSIDERED MAJOR STRENGTH OF "CAP".

EC ARGUMENTS THAT RELIABILITY OF SUPPLY MAJOR ADVANTAGE OF COMMODITY AGREEMENTS SHOULD ALSO BE WEAKENED TO SOME EXTENT BECAUSE IMMEDIATE RESPONSE OF GOF TO SHORT SUPPLY SITUATION WAS TO RESTRICT EXPORTS (POTATOES, HAY, AND SUGAR, FOR EXAMPLE).

COMMENTS:

A. A MAJOR DETERMINANT OF POLITICAL IMPLICATIONS FOR

EC AND CAP IS AVAILABILITY OF UNCOMMITTED FEOGA FUNDS TO FINANCE DROUGHT LOSSES. THUS SUGGEST THIS ANALYSIS BE CONDUCTED BY USEC BRUSSELS TO ASSIST EC POSTS IN ASSESSING FUTURE POLITICAL IMPACT.

B. GRAIN RESERVES - FROM EC BUDGET STANDPOINT, ABSENCE OF GRAIN RESERVE AGREEMENT AND HIGHER EC GRAIN STOCKS WAS BENEFICIAL IN THAT HIGHER IMPORTS INCREASED FEOGA REVENUE-LIMITED OFFICIAL USE

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NUES EVEN THOUGH INDIVIDUAL COUNTRIES' BALANCE OF PAYMENTS WERE ADVERSELY AFFECTED.

C. SUGGEST USDA ANALYZE ADVERSE EFFECT OF CAP ON EC CONSUMERS. FOR EXAMPLE, IN ABSENCE OF CAP, MEAT PRICES WOULD HAVE FALLEN IN SHORT RUN OWING TO DROUGHT INDUCED LIVESTOCK SLAUGHTER, AND IMPORTS WOULD KEEP PRICES DOWN DURING HERD BUILD-UP NEXT YEAR. DUE TO CAP, HOWEVER, CONSUMERS WILL NOT BENEFIT FROM INCREASED LIVESTOCK SLAUGHTER IN 1976, AND IT IS DOUBTFUL THAT MEAT PRICES CAN BE PREVENTED FROM INCREASING SUBSTANTIALLY NEXT YEAR.

ADDENDUM: GOF JUST ANNOUNCED (AUGUST 20) THAT GOVERNMENT IS CONSIDERING "DROUGHT TAX" ON WEALTHY TO PROVIDE HEAVY COMPENSATION FOR DROUGHT STRICKEN FARMERS. TAX WOULD BE ON INCOME OF MIDDLE AND HIGH-INCOME EARNERS. FINMIN SPOKESMAN SAID NO DECISION HAD BEEN FINALLY TAKEN ON COMPENSATION, BUT TAX SEEN AS PRACTICABLE METHOD TO RAISE UP TO 7 BILLION FF TO SAVE FARMERS FROM WORST DROUGHT IN OVER A CENTURY. GOF REPORTEDLY DOES NOT WANT TO PROVIDE AID DIRECTLY FROM BUDGET BECAUSE OF INFLATIONARY IMPLICATIONS. WE VIEW THIS REPORT, IF IT TO BE INDEED GOF POSITION, AS CLEAR EFFORT OUTFLANK CRITICISM FROM LEFT (AND ELEMENTS OF MAJORITY) AND DEMONSTRATE TO ELECTORATE THAT GISCARD REGIME RESPONSIVE IN DEED AS WELL AS IN WORD.

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